SUMMARY of COOPERATIVE CASES

FARMER COOPERATIVE SERVICE
U. S. DEPARTMENT OF AGRICULTURE
WASHINGTON, D. C.

SUMMARY NO. 68

JUNE 1956

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The comments on cases reviewed herein represent the personal opinion of the author and not necessarily the official views of the Department of Agriculture.

RECENT DECISIONS ON "AGRICULTURAL COMMODITIES" EXEMPTION IN ICC ACT

(East Texas Motor Freight Lines, Inc. v. Frozen Food Express, 76 S. Ct. 574; Frozen Food Express v. United States, 76 S. Ct. 569; Home Transfer & Storage Co. v. United States, _____ F. Supp. _____)

The Supreme Court of the United States, on April 23, 1956, in East Texas Motor Freight Lines, Inc. v. Frozen Food Express, decided that fresh and frozen dressed poultry are agricultural commodities and not manufactured products thereof within the meaning of Section 203(b)(6) of the Interstate Commerce Act. Under this holding, motor vehicles are free to carry such commodities without procuring a certificate of public convenience and necessity from the Interstate Commerce Commission. The Court relied primarily on the legislative history which reveals the Congressional intention to include ginned cotton and pasteurized milk within the terms of the agricultural exemption. A dissenting opinion was filed by Mr. Justice Burton, with whom Mr. Justice Frankfurter, Mr. Justice Minton, and Mr. Justice Harlan joined.

On the same day, the Supreme Court held in Frozen Food Express v. United States that the determination by the Interstate Commerce Commission as to the scope of the agricultural exemption in the Interstate Commerce Act (49 U.S.C. 303(b)(6)) is an order subject to judicial review. The Court stated that the determination by the Commission that a commodity is or is not an exempt agricultural commodity has an immediate and practical impact on carriers who are transporting the commodities and on shippers as well. The Court held that the order is in substance a declaratory one which touches vital interests of carriers and shippers alike and which sets the standard for shaping the manner in which an important segment of the trucking business will be done. Mr. Justice Harlan dissented on the ground that the order does not represent the final views of the Commission nor does it compel any carrier to do or refrain from doing any act.

On May 7, 1956, a statutory three-judge court, sitting at Bellingham, Washington, ruled that frozen fruits and frozen vegetables were exempt agricultural commodities and not manufactured products thereof. In reaching its decision the court relied heavily on the Supreme Court decision in the East Texas case referred to above, quoting, among other passages, the following:

> "At some point processing and manufacturing will merge. But where the commodity retains a continuing substantial identity through the processing stage we cannot say that it has been 'manufactured' within the meaning of section 203(b)(6)."

COMMODITY EXCHANGE ACT CONSTRUED IN IMPORTANT ASPECTS

(Corn Products Refining Co. v. Benson, ____F. 2d____)

Although this case did not involve a cooperative, many marketing cooperatives are engaged in operations which come within the scope of the Commodity Exchange Act. For such cooperatives the action of the United States Court of Appeals (Second Circuit) on April 13, 1956, in affirming the order of the Judicial Officer of the Department of Agriculture in this case is significant.

The order of the Judicial Officer suspended the trading privileges of Corn Products Refining Company because it exceeded the 2,000,000 bushel trading limit for corn futures contracts established pursuant to the Commodity Exchange Act. The Court upheld the Government's contention that the trading limits under the Act apply to all trading in futures contracts--not specifically exempted--and not just to speculation in price differences. The Court also upheld the Department's contentions that the purchases of corn futures contracts to offset (a) anticipated manufacturing requirements and expected sales of corn products, (b) contracts to sell corn products at a price to be determined in the future, and (c) contracts to sell corn products at a fixed price to a wholly owned subsidiary are not "bona fide hedging transactions," as defined in the statute.

The Court applied the rules of statutory construction that no provision of a statute should be rendered meaningless and superfluous, and that where a provision has been "carefully included in one place and excluded in another place in a definitional statutory provision, it should not be implied in the place omitted." The Court also "pierced the corporate veil" upon a showing of 100 percent stock ownership of the subsidiary corporation, without any further showing of control by the parent corporation.

The constitutionality of the trading limits under the commerce power was upheld, and with respect to the Fifth Amendment, the Court held that the "mere fact that a member of a regulated class suffers economic loss not shared by others in the class does not constitute per se a violation of the Fifth Amendment."

CERTIORARI DENIED IN MOE V. EARLE

On April 9, 1956, the Supreme Court of the United States announced its denial of the petition for writ of certiorari in Moe v. Earle, 226 F. 2d 583. (See Summaries No. 66, p. 1 and No. 67, p. 2.)

FTC FINALLY DISMISSES APPALACHIAN APPLE CASE

(FTC Doc. # 6041, April 16, 1956)

The Federal Trade Commission on April 16, 1956, affirmed a dismissal of charges of price fixing of raw apples by apple processors and growers in the Appalachian area.

Denying an appeal by counsel supporting the complaint, the Commission, in a per curiam opinion, adopted an order by Hearing Examiner Abner E. Lipscomb. This order also dismissed charges that the parties had agreed to formula pricing and had, by agreement, diverted apples from one purchaser to another in order to maintain agreed prices. (See Summary No. 65, p. 5.)

On appeal from the examiner's dismissal, counsel supporting the complaint had maintained that the evidence showed that during the 1950 season the processors established and maintained uniform prices paid for apples. The Commission, however, found no error in the examiner's finding to the effect that pricing departures were general and agreed with the examiner that there is "inadequate record support" for the conclusion that what price uniformity there was resulted from agreement.

In conclusion, the Commission stated that there was also insufficient record to support the additional charges of agreed formula pricing and product diversion.

COOPERATIVE PAYMENTS UNDER NEW YORK ORDER VALID

The Supreme Court on April 9 denied the petition for certiorari filed by Grant, et al., to review the judgment of the United States Court of Appeals for the District of Columbia in Grant, et al. v. Benson, et al., 229 F. 2d 765, sustaining the validity of the provisions in the New York milk order for payments to cooperative associations of producers for the performance of specified marketwide services. The Court of Appeals, in upholding the findings of fact by Secretary Benson and the 1953 amendments to the order, distinguished the Grant case from the "critically different" facts in Brannan v. Stark, 342 U.S. 451. The payments held in escrow in the Grant case total approximately $3,000,000. The subject matter of cooperative payments under a milk order has been in litigation since 1941, and was first before the Supreme Court in Stark v. Wickard, 321 U.S. 288.

TAX COURT DECISION IN AUTOMOBILE CLUB OF MICHIGAN CASE AFFIRMED

(Automobile Club of Michigan v. Commissioner of Internal Revenue, 230 F. 2d 585)

The decision in this case by the Tax Court (20 T.C. 1033) covered questions respecting the running of the statute of limitations which were set forth and discussed in Summary No. 59, page 1, as being of probable application to cooperatives under certain circumstances. The United States Court of Appeals (Sixth Circuit) in the instant case affirmed the Tax Court rulings.

PRODUCTION CREDIT ASSOCIATION RESERVES HELD REASONABLE

(Winter Garden Production Credit Ass'n v. Phinney, 139 F. Supp. 213)

It was held in this case that the Commissioner of Internal Revenue abused his discretion in allowing bad debt reserves of only .17 percent where the Production Credit Corporation, as required by law (12 U.S.C. 1331f), had fixed the reserves on a much higher basis.

The opinion in the case disposed of three cases, consolidated for trial, since they all involved the same issue although different production credit associations. In all three cases the Commissioner, acting under 26 U.S.C. 23(k), reviewed the reserves the associations had established for bad and doubtful debts and reduced the reserves. The associations paid the resulting deficiencies and then sued to recover.

Pursuant to the mandate of 12 U.S.C. 1331f, the Production Credit Corporation had prescribed the amount of reserve to be maintained. These amounts had been adopted by the boards of directors of the taxpayers.

The court said in part:

> "Taxpayers contend first that the rate fixed by Production Credit Corporation, pursuant to its statutory authority, is binding as a matter of law upon all other governmental agencies, and may not be questioned here by the Commissioner. Taxpayers point to the fact that the twelve Production Credit Corporations created under the Act, including the Production Credit Corporation of Houston, as well as the various Associations created pursuant thereto, including the two taxpayers here, are 'fiscal agents' of the

United States and are deemed to be 'instrumentalities of the United States'. They point further to the initial use of Government funds, to the statutory stock ownership plan, and to their early tax exemption as showing their close governmental affinity. Taxpayers further contend that if the rate adopted be not binding on the Commissioner as a matter of law, then as a matter of fact, under all of the facts and circumstances prevailing, the rates adopted are reasonable and proper; while the rate fixed by the Commissioner is so inadequate and unreasonable as to constitute an abuse of his discretion.

"The Government, of course, contends to the contrary. It is urged that the rate of reserve determined by the Commissioner, in the exercise of the discretion vested in him by section 23(k) (1) of Title 26, is entitled to great weight and should not be disturbed in the absence of strong evidence that the discretion was abused; and secondly, that the Commissioner's determination of a proper rate is a reasonable one.

* * * * * * *

"The determination by Production Credit Corporation of what that concern considers an appropriate reserve for bad debt figure, be it a recommendation or directive, does not in my judgment fix the figure as a matter of law, or preclude a review thereof by the Internal Revenue Service. When the associations become subject to income tax by the retirement of the Government-held stock, as did Richmond and Winter Garden in 1948, their bookkeeping, accounting and other such procedures are subject to review as are those of other taxpayers; and unduly favorable procedures may be disregarded by the Commissioner.

"That being true, the question remains as to whether the Commissioner abused his discretion and, if so, to what extent. I am convinced that he did, and that the rate which the Commissioner determined is unduly low and unrealistic. I am convinced that this is so because the Commissioner's calculation does not take into account the highly significant fact that capable farm credit agencies suffered severe bad debt losses during the early 1930's; and the taxpayers here escaped this fate by reason of the fact that they were organized during the height of the depression days and that, with negligible exception, the farmers economic condition has prospered and improved during the taxpayers' entire history."

RECENT INTERNAL REVENUE SERVICE RULINGS OF INTEREST TO COOPERATIVES

1. Transportation Tax; Grain Shipments Where Decision on Export Delayed. (Rev. Rul. 56-219; I.R.B. 1956-20, 49)

> "Where grain purchased by a company is shipped to its elevator and the determination whether the grain is to be reshipped for export or for domestic use is not made until after the grain has been placed in the company's elevator, the movement of the grain from the point of origin to the elevator is domestic in character and subject to tax on the transporation of property.

"Advice has been requested whether the tax on the transportation of property, imposed by section 3475 of the Internal Revenue Code of 1939, applies to amounts paid for the transportation of grain under the circumstances described below.

"In the instant case, the company purchases grain from farmers for delivery to its elevator located at an interior point. The company has export orders antedating the delivery of grain to the carriers at points of origin and the grades of grain specified in the orders are grades common for either export or domestic use. At the time the grain is delivered to carriers at the points of origin, it is not known by the shippers or by the company which shipments are to exported. The shipments when received by the company are commingled and stored in its elevator with other grain awaiting shipment for export and for domestic use. The majority of the grain in the elevator is used to fill domestic orders.

"Section 3475 of the Code imposes a tax upon the amount paid for the transportation of property by rail, motor vehicle, water or air from one point in the United States to another. In accordance with Subpart E of Regulations 113, the tax does not apply to an amount paid for the transportation of property in the course of exportation to a foreign destination, or shipment to a possession of the United States. Exportation does not begin until (a) a definite intention to export property is formed and (b) the property is actually put into motion for a foreign destination, or is delivered to a carrier for such transportation. Property is not considered to be in the course of exportation when it is being assembled for shipment, or is being moved to a place to be shipped, if a foreign destination is undetermined and the property has not been actually and definitely started for some foreign destination. Reshipment for export of a domestic shipment does not change the domestic shipment to foreign commerce.

"Section 143.30 of Regulations 113 provides that property will be considered to be in the course of exportation from the time of delivery to a carrier in the United States for transportation by continuous movement to a point beyond the boundaries of the United States. The export character of a shipment shall be evidenced by a contract, order, proposal of purchase or other written evidence of the intention to export, antedating the delivery of the shipment to the carrier.

"In view of the foregoing, in order for a shipment of grain to an elevator to be considered as being in the course of exportation, it must be shown (1) that prior to commencement of the movement, the shipper had in his possession (a) a contract or order calling for delivery of the grain beyond the boundaries of the United States or, (b) if the shipper is not the actual exporter, written evidence that the exporter had such a contract or order, and (2) that subsequently there was delivered at a point or points of origin in the United States the quantity and quality of grain covered by the contract, or order, to be transported by a continuous movement to the destination beyond the boundaries of the United States.

"It is held that since, under the circumstances described above, the grain is not purchased by the grain company specifically to fill the export orders held by it and the determination of whether the grain is to be reshipped for export is not made until after the grain has been placed in the company's elevator, the grain when delivered by the shippers to a carrier had not actually and definitely started for some foreign destination and is not in the course of exportation. Therefore, the movement of the grain from the points of origin to the grain company's elevator is domestic in character and amounts paid for such transportation are subject to tax on the transportation of property imposed by section 3475 of the Code."

2. Carrying Charges of Cooperative Housing Corporation. (Rev. Rul. 56-225; I.R.B. 1956-22,6)

"Where, in the case of a cooperative housing corporation, as defined in section 216(b)(1) of the Internal Revenue Code of 1954, predetermined carrying charges are collected from the tenant-stockholders in excess of the actual carrying charges paid or incurred by the corporation, any refund of such charges occurring in the same year merely results in a contra-adjustment and only the net amount of the carrying charges would be taken into the accounts of the corporation for Federal income tax purposes. However, where the excess of predetermined charges at the end of any year is not used to reduce carrying charges until a subsequent year or years, such excess constitutes income to the corporation subject to Federal income taxes in the year in which received."

3. Reporting Wages Paid for Agricultural and Nonagricultural Services. (Rev. Rul. 56-118; I.R.B. 1956-13,30)

In this revenue ruling the Internal Revenue Service outlines the procedure to be followed by farm employers, including organizations exempt from income tax under section 501(a) of the Internal Revenue Code of 1954.

Since the ruling has no specific application to farmer cooperatives, it is not being set forth in full here. However, it is considered that farmer cooperatives may wish to know of its existence.

In summary, the ruling deals with the reporting by the employers referred to above who pay "wages" for both "agriculutral labor" as defined in the Federal Insurance Contribution Act and also pay "wages" to the same employee for nonagricultural services. Such employers, the ruling states, must:

(1) segregate the "wages" for "agricultural labor" from other "wages" paid;

(2) file Form 943 reporting the Federal Insurance Contributions Act taxes due with respect to "wages" paid to employees for "agricultural labor"; and

(3) file Form 941 reporting the Federal Insurance Contributions Act taxes on, and the income taxes withheld from, the "wages" paid to the employee for other "employment."